

By email:
dale.winch@ofgem.gov.uk

Date
17 January 2022
Contact / Extension
Stephanie Anderson
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Dear Dale,

Statutory consultation on modifications to the RIIO-2 Transmission, Gas Distribution and Electricity System Operator licence conditions

This response is from SP Transmission (SPT) which holds the electricity transmission licence for the south and central Scotland. SPT is part of SP Energy Networks (SPEN) and the wider Iberdrola group. Thank you for the opportunity to respond to the statutory consultation on modifications to the RIIO-2 Transmission, Gas Distribution and Electricity System Operator licence conditions (the Licence Consultation).

We welcome the progress within this Licence Consultation, and Ofgem's constructive engagement with stakeholders following the CMA's Final Determination in the RIIO-2 appeals, in relation to the proposed modifications to address the CMA's Order. We are particularly supportive of Ofgem's proposal to use the statutory modification process under Section 11A of the Electricity Act 1989 for any decisions or changes made under Special Condition (SpC) 3.13, the Large Onshore Transmission Infrastructure (LOTI) reopener, and SpC 3.14, the Medium Sized Investment Project (MSIP) reopener, as well as giving the NARM Handbook and Network Asset Risk Workbook licence status under SpC 3.1, the NARM licence condition.

However, as we explain below, there remain some specific areas of the Licence that require amendment or further attention in order to comply with the terms of the CMA's Final Determination. This letter outlines SPT's key remaining concerns with the Licence. As part of our response to this Licence Consultation, we have also provided an updated version of Ofgem's consolidated Issues Log (**Annex A**), with SPT's latest comments highlighted in red under the Electricity Transmission and CMA Self-Mod tabs, as well as an additional SPT specific Issues Log (**Annex B**), which details new issues that SPT has identified, as part of this Licence Consultation exercise.

Evaluative Price Control Deliverables (PCDs)

As discussed in detail, during the recent Licence Drafting Working Group discussions, SPT continues to have concerns with the provisions in the licence for evaluating the outputs or consumer outcomes delivered through PCDs.

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Whilst we welcome the increased detail in the latest version of SpC 9.3 (Price Control Deliverable Reporting Requirements and Methodology Document), given the range and scope of PCDs to be delivered by licensees under the RII0-2 framework, it is simply not possible for Ofgem to clearly set out the criteria in the licence, at the required level of specificity that will inform licensees as to how Ofgem will reach certain decisions. Our particular concern is with 9.3.3(d) which states that, when evaluating partial delivery of a PCD, Ofgem will determine whether the licensee has provided a justified estimate of the “*proportion of output or Consumer Outcome delivered*”. Given that this assessment by Ofgem considers, whether the licensee’s estimation of the proportion of the output or consumer outcome delivered is justified, it remains an entirely subjective decision from Ofgem. Even in the Price Control Deliverable Reporting Requirements and Methodology Document (the PCD Methodology), para 5.4.4 does not contain any further details about how Ofgem will undertake this subjective assessment of whether the “*proportion of the output or Consumer Outcome associated with the work delivered can be robustly estimated*”.

It remains SPT’s position that Ofgem has not, and cannot, sufficiently specify the manner, time and circumstances in which it will make Evaluative PCD decisions, meaning Ofgem has not met the criteria set out in the CMA’s Final Determination to use its direction powers under s7(5)(b) of the Electricity Act 1989. Given the impossibility of being able to draft into the licence, effective criteria for what is essentially a subjective decision by Ofgem, as well as the potential financial impact of PCD amendments to licensees, SPT continues to hold the strong view that any modifications to the Evaluative PCD conditions should be made under Section 11A of the Electricity Act 1989.

Network Asset Risk Metric (NARM)

Whilst we recognise and welcome the general improvement of the drafting in the latest version of the NARM Handbook, further changes are required. We have identified these issues in the attached Issues Log (at **Annex B**). We make specific reference to Appendix 3 of the Handbook that seeks to provide an indication of the potential outcomes of the NARM Funding Adjustment and Penalty Mechanism for user input scenario data. Ofgem should provide companies with an assessment tool that truly reflects the operation of the mechanism, allowing an accurate assessment of the impact of any changes in the NARM Baseline business plan, for example, by incorporating the assessment of the Risk Sub-categories for each sector within the same tool. Additionally, there are some consistency issues between the calculation model and the description of the methodology in the NARM Handbook that must be addressed.

There remains a significant gap in defining the operation of the NARM Funding and Penalty Mechanism for the Clearly Identifiable Over-delivery and Under-delivery projects. This is recognised by Ofgem in the Information Note of 15 December 2021, that sets out the principles of setting the necessary thresholds to fully define the mechanism. Despite the ‘no surprises and transparency’ principle set out in this Note, and stating that companies should be clear from ‘as early in the process as possible’ on the levels of the threshold so they can understand the mechanism impact, the qualifying criteria will not be decided until Q3 of the second year of the Price Control at the earliest. The threshold value is the key element of the qualifying criteria

for SPT, since our business plan is project specific. This is already preventing SPT from making fully informed asset management decisions, an early finalisation of the criteria is required to ensure present and future consumers' interests are protected. As we raised in the previous consultation on the NARM Handbook in March 2021, unless the mechanism was fully defined ahead of RIIO-T2, licensees would be incentivised to simply deliver the Baseline Network Risk Outputs, as the impact on companies' allowances of any changes to the baseline plan cannot be fully assessed. This continues to be the case in the first year of the price control and, according to the proposed timescales, will be the case in the second year. This delay will limit SPT's ability to make informed decisions that will impact overall RIIO-T2 delivery due to transmission projects' delivery timescales.

SPT also seeks clarification regarding Ofgem's intention in relation to the RIIO-T2 Close Out Process as per paragraph 5.4 of the NARM Handbook. It would appear to be Ofgem's intention to develop an additional methodology for the submission requirements, timeframes and implementation. We believe the NARM Funding and Penalty mechanism is the instrument to include any further developments in relation to the operation of the mechanism and justification assessment requirements. The data submissions, as specified in Standard Licence Condition (SLC) B15, should enable Ofgem's Delivery Assessment, and the timescales are described in SpC 3.1. Should any of these licence instruments require any update or modification, the relevant modification process should be used rather than through the creation of an additional methodology.

Please do not hesitate to contact us should you wish to discuss any of the points raised in the above response.

Yours sincerely,



Stephanie Anderson
Head of Regulation
SP Energy Networks